

Merchant Card Processing Discussion
Office of the State Controller
March 1, 2011

Merchant Cards Master Services Agreement

- As a result of SB 222 in 1999, through several competitive bidding processes, OSC established a master services agreement (MSA) with First Data Merchant Services
 - To provide agencies with an enterprise solution for accepting credit/debit cards
 - Fees under the contract are some of the lowest in the country (Visa /MC actual pass-through fees plus \$.04 per transaction)
- Annually, 9 million card transactions are processed under the MSA for agencies, universities, and community colleges
- Annually, 1.5 million of the 9 million are DMV online payments for vehicle registration
 - Represent 21% of the total 7 million registrations
 - Represent 16% of the total \$309 million collected

Two Card Capture Channels Recognized by the Card Brands

- Card-Not-Present – For Web transactions
 - Requires a web capture application
 - Requires a payment gateway (e.g., Common Payment Service via ITS)
- Card-Present – For face-to-face transactions
 - Requires either POS terminals or POS software application
 - Normally does not require a payment gateway like Common Payment Service

Fees Associated With Card Processing

- Interchange and Access Fees levied by the Card Brands (Visa, MC, Amex, Discover)
 - Typically a blended rate of 1.7% for public sector (Compared to 2% + in retail industry)
 - Rate varies based upon whether card presented is a rewards card or not
- Per transaction fee of \$.04 levied by First Data Merchant Services, regardless of amount
- Capture equipment (POS terminals and/or POS software, or Web application software)
- Gateway Fee for Web transactions
 - ITS's Common Payment Service Gateway – Currently \$.28 per transaction
 - Commercial Gateway – Typically ranges from \$.20 to \$.35 per transaction
- DMV could need a Gateway to accommodate its legacy mainframe STARS application
 - Advantages to interface with STAR same as the Web application
 - Possible to have a dual system, without incurring gateway fees

Card Transaction Costs vs. Paper Transaction Costs

- For small dollar transactions, the cost of processing a paper check is generally more than the cost of processing a card transaction
 - Average paper check processing cost is \$2.00
 - Cost for a card transaction varies based upon the dollar amount of the transaction
- For large dollar transactions, the cost of a card transaction can be much more than a paper transaction (e.g., tuition payment)
- Cost Savings Different for Web Payments vs. Face-to-Face Payments
 - Web Payments – Card costs normally more than offset by savings of not processing paper
 - Eliminates staff to service persons in-line
 - Electronic posting replaces paper processing
 - Face-to-Face – Card costs are not offset by savings of not processing paper
 - Staff to service persons in-line still exists
 - Electronic posting not applicable

Funding of Card Processing Costs – Two Opposing Views

- Card processing cost should be passed on to the payer in form of a convenience fee
 - Agencies have budgetary issues, as the statutory fees collected must be deposited as revenue, and appropriations are difficult to obtain to pay the processing fees
 - The payers benefitting from using the card should incur the card processing cost, not at the expense of all citizens, some who may elect to pay by check or cash
 - The budgetary issue sometimes promotes the convenience fee levying, even if the agency's online cost is less than the mailed-in paper transaction cost (which is easier to acquire funding for)
 - A government does not have to offer the card payment option because it does not have to consider the competition factor like a retailer does
- Card processing cost should be considered as a “cost of doing business” just like any other overhead cost
 - Trends are different today than they were ten years ago
 - Nationally, credit card payments alone now comprise over half of all non-cash payments
 - Many of the younger generation do not even have a check book
 - Many individuals will not stop at a gas station if it does not accept credit cards
 - Private industry assumes 70% of individuals will pay by card, and therefore establishes its regular retail price of a product or service to cover the card processing cost
 - Poll shows that 78% of people will not pay online if levied a convenience fee, but will pay by check via mail instead (detrimental to agency's online program where less staff is needed)
 - When the majority of the citizens expect the convenience of paying for a government service by credit card as they do in the private sector, then the citizen should not have to pay for that convenience. This is referred to as the “convenience expectation factor.”

Industry Issues Pertaining to Convenience Fees

- Card Brands have different rules regarding Convenience Fees

	Visa	MasterCard	Amex	Discover
Convenience Fee – Web Online	Yes	Yes	Yes	Yes
Surcharge Fee – Face-to-Face	No	Yes	Yes	Yes
Fee based on % of dollar amount	No	Yes	Yes	Yes
Convenience Fee waived for bank draft	No	Yes	Yes	Yes

- Visa prohibits a surcharge for face-to-face transactions
- Visa requires a “flat fee only” for online payments
- Visa requires any convenience fee to be applied to all forms of online payments (including bank drafts)
- Several agencies have been threaten with fines from Visa for violation (Child Support and UNC-CH)
- Most universities do not accept Visa online due to the requirement of a flat fee only
- Visa's issue is unique to universities, due to large tuition payments. Little effect for small dollar payments

Convenience Fee Vs. Discounted Price

- A “convenience fee” is an amount above the “regular price” of a product or service
- A “discount” is an amount below the “regular price” of a product or service
- The Durbin Amendment (Part of the Wall Street Reform Act of 2010) specifically allows for a “discount” if paying by check or cash, but does not address “convenience fees.”
- Discounting has different effects for “online” vs. “face-to-face”
 - Beneficial for a face-to-face transaction (allows discount off of regular price if paying by check)
 - Detrimental for a Web transaction (discount for paying by check would inhibit online payments)

Department of Administration State Portal Plans

- The DOA is currently considering securing the services of a vendor to replace the current State Web Portal utilizing the “self-funded model.”
- Such funding model allows for the levying of convenience fees, in certain cases, to fund the development and operation of the portal

Typical Fee Scenarios

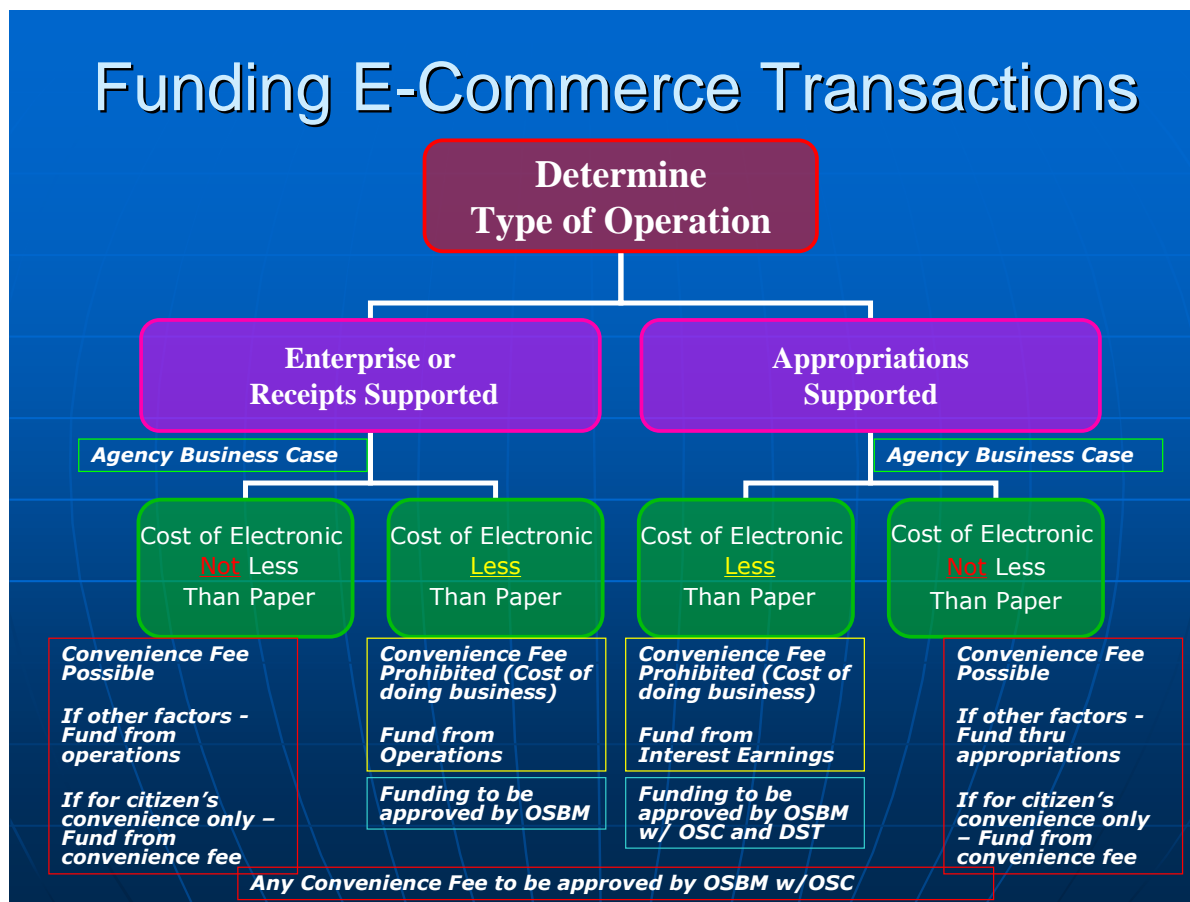
- Some cost components are based on the “per transaction”
- Some cost components are based on the “transaction amount.”
- The “interchange” component would be higher if a “reward card” is presented by the payer
- Fees below do not include ITS’s gateway per transaction fee of \$.28

Typical Fees for a \$30.00 transaction – Applying Card Associations’ best government rates										
	Visa		MasterCard		Amex		Discover		PIN Debit (NYCE) *	
	Fee	Amount	Fee	Amount	Fee	Amount	Fee	Amount	Fee	Amount
Transaction		\$30.00		\$30.00		\$30.00		\$30.00		\$30.00
Interchange-%	1.43%	.43	1.55%	.43	2.15%	.65	1.60%	.48	.75%	.23
Interchange-\$	\$.05	.05	\$.10	.10	-	-	-	-	.17	.17
Assessment-%	.0925%	.03	.1100%	.03	-	-	-	-	-	-
Access Fee-\$	\$.022	.02	\$.021	.02	-	-	-	-	-	-
Switch Fee-\$	-	-	-	-	-	-	-	-	\$.0425	.04
STMS-\$	\$.04	.04	\$.04	.04	\$.04	.04	\$.04	.04	\$.04	.04
Total Fee		\$.57		\$.58		\$.69		\$.52		\$.48

Typical Fees for a \$300.00 transaction – Applying Card Associations’ best government rates										
	Visa		MasterCard		Amex		Discover		PIN Debit (NYCE)	
	Fee	Amount	Fee	Amount	Fee	Amount	Fee	Amount	Fee	Amount
Transaction		\$300.00		\$300.00		\$300.00		\$300.00		\$300.00
Interchange-%	1.43%	4.29	1.55%	4.65	2.15%	6.45	1.60%	4.80	.75%	2.25
Interchange-\$	\$.05	.05	\$.10	.10	-	-	-	-	.17	.17
Assessment-%	.0925%	.28	.1100%	.33	-	-	-	-	-	-
Access Fee-\$	\$.022	.02	\$.021	.02	-	-	-	-	-	-
Switch Fee-\$	-	-	-	-	-	-	-	-	\$.0425	.04
STMS-\$	\$.04	.04	\$.04	.04	\$.04	.04	\$.04	.04	\$.04	.04
Total Fee		\$4.68		\$5.14		\$6.49		\$4.84		\$2.50

Electronic Commerce Task Force Report - 2008

- Can be viewed at <http://www.osc.nc.gov/financial/index.html>
- Addresses the issues in detail
- Contained recommendations regarding when convenience fee should be levied
 - When cost of electronic less than paper – Do not levy a convenience fee
 - When cost of electronic more than paper – Consider levying a convenience fee



Factors Considered for Absorbing Fees as a “Cost of Doing Business”

- Reduced transaction costs
- Speedier collections and availability of funds (increased interest earnings)
- Payment for service or product is considered “mandatory” (e.g., taxes)
- Acceptance of an electronic transaction would likely increase sales or revenue
- Payment is to satisfy a “delinquent” account or other type of payment that would not likely otherwise be collected
- Other factors deemed appropriate for a particular type of payment (e.g., convenience expectation of citizen)